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SUBJECT: SLOVENIA: ENERGY SECURITY AND HYDROELECTRIC POWER

REF: LJUBLJANA 0171

SENSITIVE

11. (SBU) Summary: Companies within the state-owned Holding Slovenske Elektranar (HSE) group produce over half of Slovenia's electricity. With the GOS looking for self-sufficiency in electricity, HSE's further construction of hydroelectric plants will play a key role. HSE is currently evaluating plans to develop two major natural gas-fired facilities, one in Slovenia and one in Austria, in a partnership between HSE, a Slovenian manufacturer, and an Austrian corporation. Privatization of HSE, however, does not appear to be high on its or the GOS's agenda, despite interest from a major German power producer. Following is an overview of a recent visit by DCM to HSE and one of its subsidiary companies. End summary.

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What is HSE?  
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12. (U) In July 2001, the GOS established HSE as an integrated entity of three hydroelectric plants (Dravske, Savske, and Soske), two coal-fired electricity plants (Brestanica and Sostanj) and a coal mine located in Velenje. Today, HSE is the leading Slovenian power producer, comprised of ten companies and more than five thousand employees. HSE companies produce more than 50 percent of all electricity generated in Slovenia. (Note: the Krsko nuclear power plant is not/not part of HSE.) Owned by the state of Slovenia, in 2005 HSE reported approximately USD 74 million in pre-tax profit. The company receives nearly all of its revenue from buying and selling electricity and does not own or manage distribution networks.

13. (U) One of the key components of HSE's business and Slovenia's energy strategy is hydroelectric power. Hydropower has been supplying electricity to the residents of Slovenia since the construction of the Medvode hydro plant, part of the HSE subsidiary Savske Elektranar. The 20MW facility, originally built in the 1950s and currently undergoing a multi-year restoration, is located in the suburbs of Ljubljana. As noted reftel, hydroelectric plants on the Sava, Drava, and Soca rivers provide approximately one-third of the electricity that is consumed in Slovenia. HSE controls all of the companies that produce hydroelectric

power in Slovenia.

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Independence in Electricity  
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¶4. (U) During a visit to HSE, CEO Jozse Zagozen told DCM that it plans to invest between 1.3 and 2.9 billion Euros in the coming decade to develop and expand electrical production in Slovenia. Per reftel, Slovenia currently imports approximately 10-15 percent of its electricity. Zagozen said that the goal of HSE and the GOS is to reach self-sufficiency in electrical production. He estimates that the planned investment in increased capacity and improved efficiency in both coal and hydro facilities will achieve that objective. (Note: Although HSE imports electricity from neighboring states, it also exports approximately 300MW to Italy because of the higher prices it can charge.)

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Hydroelectric Power to Increase  
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¶5. (U) Zagozen noted that while the GOS will invest significant resources to modernize the major coal-fired facilities in Slovenia, hydroelectric power is an important element of Slovenia's electricity production strategy. One of the few natural resources that Slovenia can draw on, Zagozen said the strong water flow on Slovenia's major rivers is an asset that HSE must continue to develop. Echoing what Post has learned from other sources, Zagozen told DCM he felt that an ideal strategy would achieve a share of 35 to 40 percent of Slovenia's overall electrical needs from its hydroelectric plants. Despite the relatively

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high investment required to build a hydro plant (three times that of coal per installed megawatt), Zagozen said that accelerated development of plants along the Soca, Drava, Sava, and Mura rivers was necessary if Slovenia is to achieve and maintain self-sufficiency in electricity production.

¶6. (U) During a visit to the Medvode facility of Savske Elektrarne, the HSE firm that operates hydroelectric plants along the Sava River, Managing Director Drago Polak told DCM that he also expects continued, significant development of hydro resources in Slovenia. Polak said that only 12 percent of the total available potential of the Sava River has been developed, and that plans to take advantage of this resource are underway. He added that in the coming 10-15 years, 15 more hydro plants are planned to be built on the Sava. Polak said that the power of the Sava river largely depends on runoff from Alpine snowfall and, thanks to this year's very heavy snowfall, the Sava plants would be uncharacteristically productive in the spring and early summer months of 2006.

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Natural Gas An Option?  
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¶7. (SBU) Zagozen told DCM that HSE is currently investigating the possibility of investing in natural gas-fired electrical facilities. Noting that Slovenia currently receives a very small percentage of its electricity from natural gas, Zagozen said these proposed plants could be one way of diversifying production. Post understands that HSE, Talum (a Slovenian aluminum producer), and an Austrian company called Verbund have established a joint venture company to conduct feasibility studies of two proposed 400MW plants, one in Kidricevo in northeastern Slovenia and a similar facility in Austria. Construction of a plant of this size in Slovenia would require redevelopment of existing gas lines, which are insufficient to transport the 1 billion cubic meters of gas which a plant of this size

would need annually. Zagozen noted that any decision to move forward on a gas-fired facility in Slovenia would depend on the results of a risk analysis of increasing sourcing of natural gas from Russia. (Note: Slovenia imports approximately 60 percent of its natural gas needs from Russia. Most of this is used for heating and industrial purposes.)

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HSE Privatization?  
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18. (SBU) The GOS has said that it intends to sell off at least part of HSE and create another major energy producer to improve the competitiveness of the market (reftel). German energy corporation E.ON has expressed interest in a possible purchase of 25 percent or more of HSE and would provide capital to achieve the goals of HSE's development strategy. Concrete plans for privatization, however, have yet to materialize and high-ranking GOS officials have indicated that they will move conservatively. As he has said in public fora in the past, Zagozen does not believe that privatization is a panacea to better competition and that HSE currently has the "optimal combination of resources." Zagozen acknowledged that privatization could bring some benefits, but he does not believe that the individual companies within the HSE group should be sold off. Synergies within the group must be maintained, Zagozen said, and if there is any privatization, the "state should remain the majority owner."

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Comment  
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19. (SBU) The diversity of supply and operational stability of HSE bode well for the future of electricity security in Slovenia. Further development of hydropower as an energy resource will be a critical part of Slovenia's energy strategy and, in light of only muted expressions of concern from environmentalists, appears to be on track. In view of

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the Russia-Ukraine natural gas dispute from January, HSE's investigation of a possible increase in gas usage is worth noting. Post contacts tell us that these plans are, however, only in the early investigative stages and may well never come to fruition. End comment.  
ROBERTSON